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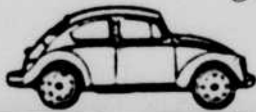

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Speaker sees inflation for future

Bad policies to take their toll on economy

By Dan Eisler
Emerald Reporter

For the past nine years, the Federal Reserve Board, the president and Congress have been playing a game of financial chicken that is sending the United States on the road toward hyperinflation, said economist Tom Sargent.

Sargent, speaking Thursday at a Willamette Hall lecture titled "Interpreting the Reagan Deficits," said U.S. monetary and fiscal policies have been at odds with each other since Reagan became president in 1981.

If the government continues its current rate of borrowing instead of raising taxes or cutting expenditures, it will eventually run out of willing lenders and have to resort to printing money to finance itself, Sargent said.

"It's tempting to think we can't do what banana republics do, that we're so big somehow we're never going to have inflations," Sargent said, pointing out that big countries have experienced high inflation in the past, including France during its revolution and Germany after World War I.

"Those inflations weren't brought about by magic but by arithmetic, and the United States faces the same arithmetic.

"Arithmetic says if you're going to run a permanent government deficit, then you're going to have to have, on some average basis, money creation that's going to generate enough inflation to cover that deficit," Sargent said.

"On the other hand, if you want to have a zero inflation policy (or) no monetary growth, what you're going to need is the balanced budget, in a present value sense; that is, deficits now are accompanied by surpluses in the future," he said.

Sargent said the pre-tax, real interest rate on government debt exceeded the U.S. economic growth rate for the first time after Reagan took office.

"It means even if you don't run a new deficit, your debt's going to be growing, relative to the size of the economy, just because of the arithmetic of compounding," Sargent said.

Just financing the interest payments will increase the debt, he said.

Moreover, the debt is actually higher than reported, because a $60 to $70 billion Social Security trust fund surplus is added to make the debt look smaller, Sargent said.

Lyndon Johnson was the first president to claim to reduce the deficit when all he really did was combine books, Sargent said. "Johnson did that and made it stick."

The Reagan administration promised to stamp out inflation by having the Federal Reserve continue a tight money policy, reducing taxes, maintaining the existing size of the government and balancing the budget within four years, Sargent said.

"These promises don't make sense," Sargent said. "They violate arithmetic. If you're going to cut taxes and leave government expenditures the same, it implies you're going to have a string of government deficits.

"If you're going to do that on a permanent basis; that is, you're not promising to reduce taxes now and increase them later, you're saying you're going to have a permanent reduction in taxes," Sargent said.

"That's not honest," Sargent said. "And that's a promise George Bush endorsed when he said, 'No new taxes.' "

That implies if expenditures aren't reduced, the government will have to print more money to finance them, Sargent added.

"On the other hand, the claim that you're going to fight inflation and encourage (Reagan's Reserve chairman Paul) Volcker and his successors to keep money tight is only a feasible promise if the government budget is going to be balanced," Sargent said.

Sargent is a senior research fellow at the Hoover Institute, a conservative think-tank at Stanford University in California, and an adviser to the Federal Reserve Bank in Minneapolis.

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